

36



NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

In re:)	Case No. 11-37711-B-7
)	
DELANO RETAIL PARTNERS, LLC,)	Adversary No. 16-2146
)	
)	DC Nos. HSM-1
Debtor.)	DBR-1

SUSAN K. SMITH, Chapter 7
Trustee,

Plaintiff,

v.

C&S WHOLESALE GROCERS, INC., a
Vermont Corporation,

Defendant.

C&S WHOLESALE GROCERS, INC., a
Vermont Corporation,

Counterclaimant,

v.

SUSAN K. SMITH, Chapter 7
Trustee,

Counterdefendant.

MEMORANDUM DECISION GRANTING TRUSTEE'S MOTION FOR SUMMARY
JUDGMENT AND DENYING C&S's MOTION FOR SUMMARY JUDGMENT

1 INTRODUCTION

2 There are two motions for summary judgment presently before
3 the court. Plaintiff Susan K. Smith, in her capacity as the
4 trustee appointed in the parent chapter 7 case ("Trustee")
5 captioned In re Delano Retail Partners, LLC, case no. 11-37711,
6 filed one summary judgment motion. Defendant C&S Wholesale
7 Grocers, Inc. ("C&S"), a purported secured creditor in the parent
8 chapter 7 case, filed the other.

9 Delano Retail Partners, LLC ("DRP") is the debtor in the
10 parent chapter 7 case. Dennis Delano and Harley Delano
11 ("Delanos") are the managers of DRP. DRP's attorney was Joseph
12 Neri ("Neri"). The Delanos also formed another entity by the
13 name of 2040 Fairfax, Inc. ("2040 FF"). The relationship of the
14 parties and these entities is discussed in greater detail below.

15 The Trustee commenced this adversary proceeding by filing a
16 complaint on July 22, 2016. The first four claims for relief in
17 that complaint are for declaratory relief. For lack of a better
18 description, those claims concern funds identified as four
19 "buckets" of money which consist of the following:

- 20 (1) approximately \$429,505.00 received or to be
21 received from the settlement of the estate's
22 claims against the Delanos, 2040 FF, and Neri that
23 C&S purchased from the Trustee, thereafter
24 prosecuted, and ultimately settled (the
25 "Settlement Funds");
- 26 (2) approximately \$384,000.00 of an original balance of
27 approximately \$560,000.00 that DRP transferred from its
28 bank account to Neri's client trust account prepetition
and which thereafter was transferred from Neri's client
trust account to the Trustee (the "Neri Trust Account
Funds");
- (3) approximately \$153,410.08 the Trustee collected
from 2040 FF postpetition for 2040 FF's lease of
DRP's furniture, fixtures, and equipment under a

1 prepetition asset lease agreement (the "Asset
2 Lease Payments"); and

- 3 (4) approximately \$37,661.60 the Trustee received from
4 the sale of DRP's liquor licenses (the "Liquor
5 License Proceeds").

6 The Trustee seeks a declaration that the funds in each of
7 the "buckets" are not subject to C&S's prepetition security
8 interest and therefore belong to the estate free and clear. The
9 fifth claim for relief in the complaint is a claim under 11
10 U.S.C. § 542(a) for turnover of the Settlement Funds.

11 C&S filed an answer and counterclaim on September 6, 2016.
12 The counterclaim asserts the same four claims for declaratory
13 relief that are asserted in the complaint (but in different
14 order). It seeks a declaration opposite of that requested in the
15 complaint. In other words, whereas the Trustee seeks a
16 declaration that all of the funds in each of the four above-
17 referenced "buckets" are not subject to C&S's prepetition
18 security interest, C&S seeks a declaration that all of the funds
19 in each of those "buckets" are subject to its prepetition
20 security interest.

21 The Trustee filed the initial summary judgment motion on May
22 5, 2017. C&S opposed the Trustee's summary judgment motion on
23 May 23, 2017, and the Trustee replied on May 30, 2017. C&S filed
24 a memorandum of points and authorities on May 5, 2017, and its
25 summary judgment motion on May 9, 2017. The Trustee opposed
26 C&S's summary judgment motion on May 23, 2017, and C&S replied on
27 May 30, 2017. A hearing on the parties' cross-motions for
28 summary judgment was held on June 9, 2017. Appearances at that
 hearing were noted on the record.

1 In reaching its decision, the court has reviewed and
2 considered the following documents: (i) with regard to the
3 Trustee's summary judgment motion, docket nos. 32-39, 49-56, 64-
4 70, 76, 82, 86 & 89; and (ii) with regard to C&S's summary
5 judgment motion, docket nos. 40-48, 57-63, 71-74, 75, 83, 86 &
6 88. The court also takes judicial notice of the dockets in this
7 adversary proceeding and in the parent chapter 7 case, the
8 dockets in related adversary proceedings nos. 12-02686 and 13-
9 02250 filed in this court, and the dockets in related case nos.
10 2:13-cv-01413-TLN-AC, 2:14-cv-02215-TLN-DAD, and 2:14-cv-02263-
11 TLN filed in the district court.¹ The court has also relied on
12 the parties' stipulated undisputed facts and facts the parties
13 submitted that the court has discerned are not in dispute.²

15 **FACTUAL BACKGROUND**

16 I. Generally

17 C&S is a grocery wholesaler that sold store inventory to DRP
18 before DRP filed its voluntary chapter 7 petition. In 2006 C&S
19 and DRP executed a supply agreement, promissory note, and
20 security agreement. In connection with those agreements, C&S
21 loaned DRP \$2,000,000.00 to purchase assets and equipment for
22 stores, including stores that DRP acquired from Ralph's Grocery
23 Company and specifically including a store located at 2040 Sir
24

25 ¹The requests for judicial notice at dkts. 44, 53, & 60 are
26 granted.

27 ²Except for plaintiff's objection 1.a. [dkt. 59] which is
28 sustained inasmuch as it is not necessary for the court to reach
the "equities of the case issue," all other objections at dkts.
51 and 59 are overruled.

1 Francis Drake Blvd., Fairfax, California.

2 The loan from C&S to DRP is evidenced by the promissory
3 note, which is secured by the security agreement. The security
4 agreement grants C&S a security interest in numerous classes of
5 DRP's assets, all of which are identified in the security
6 agreement submitted as an exhibit to the motion. Relevant here
7 are all claims, accounts, general intangibles, chattel paper,
8 deposit accounts, leases, inventory, furniture, fixtures, and
9 equipment, and all proceeds of the foregoing. C&S's security
10 interest in this collateral is perfected by a UCC-1 financing and
11 two continuation statements.

12
13 II. As Specifically Relating to Each of the Four "Buckets"

14 A. The Settlement Funds: Trustee's First Claim for Relief
15 in the Complaint & C&S's Fourth Claim for Relief in the
Counterclaim [\$429,505.00]

16 In November 2012 C&S filed an adversary complaint that named
17 the Delanos, 2040 FF, and Neri as defendants. That complaint
18 alleged fraudulent transfer claims, and claims for conspiracy to
19 commit and aiding and abetting in the commission of fraudulent
20 transfers.

21 In March 2013 the Delanos, 2040 FF, and Neri moved to
22 dismiss the adversary complaint. Those defendants asserted that
23 the claims alleged in the complaint belonged to the estate and
24 therefore C&S lacked standing to prosecute them on its own
25 behalf. The Trustee also asserted ownership of the claims.
26 After C&S moved in April 2013 to prosecute the estate's claims in
27 place of the Trustee and for the benefit of the estate, C&S and
28 the Trustee entered into a stipulation in May of 2013 that

1 authorized C&S to prosecute the estate's claims, including those
2 alleged in the 2012 adversary complaint. There are two
3 significant paragraphs in that stipulation.

4 The first is ¶ 1 which pertains to the consideration that
5 C&S agreed to pay the Trustee for its purchase—and the Trustee's
6 sale—of the estate's claims. Paragraph 1 states that "in
7 consideration of payment to the Trustee for the benefit of DRP's
8 estate out of any settlement, judgment or other recovery" C&S
9 would pay the Trustee (i) a minimum of \$250,000.00, (ii) an
10 additional \$50,000.00 of any amount between \$300,000.00 and
11 \$1,000,000.00, and (iii) the \$250,000.00 and the \$50,000.00 plus
12 25% of any amount over \$1,000,000.00.

13 The second is ¶ 3 which states as follows:

14 The terms for payment as set forth herein shall be
15 without prejudice to, and shall not affect, C&S'
16 assertion of any secured and unsecured claims herein,
17 as well as the Trustee's right to dispute, contest, or
otherwise object to any such claims, all of which
rights and remedies are hereby preserved and unaffected
by this stipulation.

18 The Trustee filed a motion to approve the stipulation in May
19 2013. The court (Holman, J.) heard that motion on June 18, 2013,
20 and also treated it as a motion to sell the estate's claims to
21 C&S. During the hearing on the motion, and without any objection
22 from or disagreement by C&S, the Trustee explained ¶ 3 of the
23 stipulation as follows:

24 And as the trustee made clear in her reply to the
25 Fund's opposition, the ability to object to C&S's **claim**
26 is preserved to the estate. All rights are reserved
27 here. If the trustee feels that there has been some
28 sort of double dipping or double recovery to C&S as a
result of the litigation, she retains the ability under
the Bankruptcy Code to object to that **proof of claim**
and will do so if that serves the interest of the
estate.

1 Hr'g Tr. at 6:9-17 (emphasis added).

2 The order granting the motion and approving the May 2013
3 stipulation and sale of the estate's claims to C&S was entered in
4 July 2013. Thereafter, C&S owned 100% of the estate's claims and
5 it asserted its ownership of those claims in pleadings filed in
6 subsequent litigation involving the purchased claims. C&S also
7 characterizes all of the claims it bought from the estate as its
8 collateral and the proceeds received in settlement of the
9 estate's claims as a replacement for its damaged or destroyed
10 collateral.

11 C&S settled the estate's claims against the Delanos and 2040
12 FF in January of 2015. That settlement agreement requires 2040
13 FF to make 42 monthly payments of \$10,833.00 each from February
14 2015 to July 2018, with increasing payments thereafter to and
15 including January 2022. Under that settlement agreement, 2040 FF
16 agreed to pay a total of \$1,518,020.00 to C&S by January 2022.
17 C&S also settled the estate's claims against Neri in July of
18 2015. That settlement agreement requires Neri to pay \$40,000.00.
19 Based on the amounts of those settlements, \$429,505.00 is at
20 issue with regard to this "bucket".

21
22 B. Neri Trust Account Funds: Trustee's Fourth Claim for
23 Relief in the Complaint and C&S's First Claim for
24 Relief in the Counterclaim [\$384,000.00]

25 From 2009 to 2010, several of DRP's grocery stores in
26 Northern California experienced a downturn in business and began
27 shutting down. As the remaining DRP stores (other than Fairfax)
28 went out of business, DRP sold inventory.

In late 2010, DRP transferred \$560,000.00 from its bank

1 account to Neri's client trust account. There is also deposition
2 testimony that inventory proceeds were deposited into Neri's
3 client trust account in late 2010. That same deposition
4 testimony also reflects that whatever the extent of inventory
5 proceeds that went into Neri's client trust account, those
6 proceeds were not segregated and, in fact, were commingled with
7 other funds that belonged to a "Peterson" and other unidentified
8 operational funds.

9 In any case, of the \$560,000.00 that was deposited into
10 Neri's client trust account in late 2010, \$384,000.00 was
11 transferred from Neri's client trust account to the Trustee in
12 July 2011. The reduction resulted from withdrawals from the
13 trust account to pay DRP's taxes, payroll, and employment
14 department claims. An order entered in prepetition state court
15 litigation also authorized a withdraw from the account to pay
16 expenses associated with that litigation.

17
18 C. Asset Lease Funds: Trustee's Third Claim for Relief in
19 the Complaint & C&S's Second Claim for Relief in the
Counterclaim [\$153,410.08]

20 In 2008 the Delanos formed 2040 FF with Neri's assistance.
21 DRP terminated its rights under an existing sublease of the
22 Fairfax store and, simultaneously, 2040 FF negotiated a new long-
23 term lease for that store. DRP and 2040 FF executed a sublease
24 agreement for the Fairfax store under which DRP agreed to pay the
25 monthly rent due under 2040 FF's new long-term lease. DRP and
26 2040 FF also executed an agreement under which DRP agreed to use
27 its license, permits, employees, and other resources to operate
28 the Fairfax store on behalf of 2040 FF.

1 Relevant for purposes of this "bucket" is that in January
2 2010 DRP entered into what is referred to as an "Asset Lease"
3 with 2040 FF under which DRP leased its furniture, fixtures, and
4 equipment in the Fairfax Store to 2040 FF in exchange for semi-
5 annual payments from 2040 FF. After DRP filed its chapter 7
6 petition, payments under the Asset Lease were collected directly
7 by the Trustee. Prepetition those payments were made to DRP.
8 The Trustee has collected approximately \$153,410.08.

9
10 D. Liquor License Sale Funds: Trustee's Second Claim for
11 Relief in the Complaint & C&S Third Claim for Relief in
the Counterclaim [\$37,661.60]

12 DRP owned several liquor licenses which were used in
13 connection with grocery store operations. The Trustee sold those
14 liquor licenses to third parties during the administration of the
15 bankruptcy case. The Trustee received net sales proceeds of
16 approximately \$37,661.60 from those sales. C&S claims those
17 funds as proceeds of its collateral consisting not of the liquor
18 licenses themselves but, rather, as proceeds of the liquor
19 licenses as general intangibles.

20
21 **JURISDICTION**

22 Federal subject matter jurisdiction is founded on 28 U.S.C.
23 § 1334. This adversary proceeding is a core proceeding under 28
24 U.S.C. §§ 157(b)(2) (A), (B), (E), (K), and (O). To the extent
25 this adversary proceeding may ever be determined to be a matter
26 that a bankruptcy judge may not hear and determine without
27 consent, the parties nevertheless consent to such determination
28 by a bankruptcy judge. See 28 U.S.C. § 157(c)(2). Venue is

1 proper under 28 U.S.C. § 1409.

2
3 **LEGAL STANDARD**

4 Summary judgment is proper where "the pleadings,
5 depositions, answers to interrogatories, and admissions on file,
6 together with the affidavits, if any, show that there is no
7 genuine issue as to any material fact and that the moving party
8 is entitled to a judgment as a matter of law." Fed. R. Civ. P.
9 56(c); Fed. R. Bankr. P. 7056. The moving party has the burden
10 of demonstrating the absence of a genuine issue of fact.

11 Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 256 (1986). That
12 burden may be discharged by showing, i.e., pointing out, that
13 there is an absence of evidence to support the nonmoving party's
14 case. Celotex Corp. v. Catrett, 477 U.S. 317, 322 (1986).
15 Thereafter, the nonmoving party bears the burden of designating
16 specific facts demonstrating genuine issues for trial. In re
17 Oracle Corp. Sec. Litig., 627 F.3d 376, 387 (9th Cir. 2010).

18 In examining a motion for summary judgment, "the inferences
19 to be drawn from the underlying facts . . . must be viewed in the
20 light most favorable to the party opposing the motion." U.S. v.
21 Diebold, Inc., 369 U.S. 654, 655 (1962). However, the nonmoving
22 party's allegation that factual disputes persist will not
23 automatically defeat an otherwise properly supported motion for
24 summary judgment. See Fed. R. Civ. P. 56(e). And a "mere
25 'scintilla' of evidence will be insufficient to defeat a properly
26 supported motion for summary judgment; instead, the nonmoving
27 party must introduce some 'significant probative evidence tending
28 to support the complaint.'" Fazio v. City & County of San

1 Francisco, 125 F.3d 1328, 1331 (9th Cir. 1997) (quoting Anderson,
2 477 U.S. at 249, 252). The court does not weigh conflicting
3 evidence; rather, it asks whether the nonmoving party has
4 produced sufficient evidence to permit the factfinder to hold in
5 its favor. Ingram v. Martin Marietta Long Term Disability Income
6 Plan for Salaried Employees of Transferred GE Operations, 244
7 F.3d 1109, 1114 (9th Cir. 2001).

8 Cross-motions for summary judgment evaluated separately,
9 giving the nonmoving party in each instance the benefit of all
10 reasonable inferences. A.C.L.U. of Nev. v. City of Las Vegas, 466
11 F.3d 784, 790-91 (9th Cir. 2006) (quotation marks and citation
12 omitted); Pintos v. Pac. Creditors Ass'n, 605 F.3d 665, 674 (9th
13 Cir. 2010). In evaluating the motions, "the court must consider
14 each party's evidence, regardless under which motion the evidence
15 is offered." Las Vegas Sands, LLC v. Nehme, 632 F.3d 526, 532
16 (9th Cir. 2011).

17 18 DISCUSSION

19 I. The Cross-Motions for Summary Judgment

20 A. The Settlement Funds are not Collateral or Proceeds 21 that Replace Damaged or Destroyed Collateral.

22 This "bucket" contains the proceeds received and to be
23 received in settlement of the estate's claims against the
24 Delanos, 2040 FF, and Neri. C&S maintains those funds, including
25 the consideration it is obligated to pay the Trustee for its
26 purchase of those claims from the Trustee, are encumbered by its
27 security interest either as its collateral, i.e., the claims, or
28 as the replacement of damaged or destroyed collateral, i.e., the

1 settlement proceeds. The Trustee, on the hand, maintains that
2 the consideration portion of the Settlement Funds are not subject
3 to any security interest. For the reasons explained below, the
4 Trustee is correct.

5 It is true that DRP granted C&S a security interest in "all
6 claims." It is also true that settlement proceeds can be a
7 replacement for original collateral that is damaged or destroyed.
8 O.H. Kruse Grain and Milling v. United California Bank (In re
9 Wiersma), 324 B.R. 92, 106 (9th Cir. BAP 2005), aff'd in part,
10 rev'd in part, 483 F.3d 933 (9th Cir. 2007), and aff'd in part,
11 277 Fed. Appx. 603 (9th Cir. 2007); In re Endresen, 530 B.R. 856,
12 869 (Bankr. D. Or. 2015), aff'd in part, rev'd in part, 548 B.R.
13 258 (9th Cir. BAP 2016). However, at least in this case, an
14 admission by C&S negates the possibility of any such outcome.

15 The Trustee cites In re Ice Mgmt. Sys., Inc., 2014 WL
16 6892739 (9th Cir. BAP 2014), for the proposition that the portion
17 of the Settlement Funds described in the May 2013 stipulation as
18 the consideration C&S is obligated to pay the Trustee for its
19 purchase of the estate's claims are not encumbered by C&S's
20 prepetition security interest. In an effort to distinguish Ice
21 Management from this case, and to refute the Trustee's argument,
22 C&S makes the following statement which the court treats as an
23 admission:³

24
25 ³The court exercises its discretion to treat the statement
26 as an admission. See American Title Ins. Co. v. Lacelaw Corp.,
27 861 F.2d 224, 227 (9th Cir. 1988). The statement was not
28 inadvertent. It was made in the context of a request by C&S for
affirmative relief. The court pointed out the statement to C&S's
attorney when the parties' summary judgment motions were heard on
June 9, 2016, and since that time C&S has not amended, retracted,
or assigned any error to the statement. See Sicor Ltd. v. Cetus

1 Unlike in *Ice*, the Trustee here did not sell an
2 encumbered asset, such as an intellectual property
3 right belonging to DRP or, for example, an item of real
4 or personal property that was subject to an existing
5 lien or security interest. Rather, *the Trustee sold*
6 *the Estate's claims-claims* that only *she* had standing
7 to prosecute.

8 Dkt. 71 at 9:8-12 (emphasis in original).

9 Short of buying claims from the same individual who sold
10 Jack his magic beanstalk beans, the admission that the estate's
11 claims, *i.e.*, the very claims that C&S bought from the Trustee,
12 prosecuted, and settled resulting in the Settlement Funds, are
13 not (and when bought were not) encumbered can only mean those
14 claims are not (and when bought were not) subject to any security
15 interest under the security agreement between C&S and DRP. That
16 means the claims are not (and could not be) collateral. That
17 also means proceeds received in settlement of the unencumbered
18 claims likewise are not (and could not be) a replacement for
19 original collateral-damaged, destroyed, or otherwise.

20 The admission by C&S that the Trustee did not sell it
21 encumbered claims also sheds light on the purpose of ¶ 3 of the
22 May 2013 stipulation. The purpose of that paragraph could not be
23 to preserve a security interest in the consideration portion of
24 the Settlement Funds - or any portion of the Settlement Funds for
25 that matter - because the paragraph cannot be read to preserve

26 Corp., 51 F.3d 848, 859-860 (9th Cir.), cert. denied, 116 S.Ct.
27 170 (1995) (stating that where "the party making an ostensible
28 judicial admission explains the error in a subsequent pleading or
by amendment, the trial court must accord the explanation due
weight"); see also Westgate Communications, LLC v. Chelen County,
Fed. Appx. 708 (9th Cir. 2013) (district court properly declined
to treat statement in memorandum as admission where statement was
read out of context, inadvertent, party making statement timely
confessed error, and statement retracted).

1 that which C&S admits does not (and when it bought the estate's
2 claims from the Trustee did not) exist, i.e., a security
3 interest.

4 The Trustee's statements during the hearing on the motion to
5 approve the stipulation and sale of the estate's claims to C&S
6 are also independent evidence that the purpose of ¶ 3 of the May
7 2013 stipulation was not to preserve any security interest.
8 Rather, as the Trustee explained, the purpose of that paragraph
9 was to preserve the secured and unsecured claims that C&S
10 asserted in its proof of claim and the Trustee's ability to
11 object to the proof of claim to prevent a double recovery by C&S
12 on both the proof of claim and the estate's claims. C&S did not
13 object to or otherwise dispute the Trustee's explanation of ¶ 3
14 when it was given. And it does not do so now with any admissible
15 evidence.

16 Finally, it is also worth noting that the motion to approve
17 the stipulation and Trustee's sale of the estate's claims to C&S
18 was considered in the context of the Woodson and A&C factors.⁴
19 That standard requires the court to find that a proposed
20 settlement and compromise provides some benefit to the estate and
21 creditors. If Judge Holman understood that the consideration C&S
22 agreed to pay the Trustee for its purchase of the estate's claims
23 was subject in its entirety to a security interest so that the
24 estate effectively received nothing in exchange for the sale of
25 its claims to C&S, he could not have found that the stipulation
26

27 ⁴Woodson v. Fireman's Fund Ins. Co. (In re Woodson), 839
28 F.2d 610 (9th Cir. 1988); Martin v. Kane (In re A&C Properties),
784 F.2d 1377 (9th Cir. 1986).

1 and motion to approve it satisfied the Woodson and A&C factors.

2 The benefit to the estate from the stipulation and the
3 Trustee's sale of the estate's claims to C&S comes in the form of
4 the "consideration" that C&S is now obligated to pay the Trustee
5 for its purchase of the estate's claims. That consideration is a
6 clearly-defined structured payment arrangement pursuant to which
7 C&S is obligated to pay the Trustee a total of \$429,505.00. In
8 other words, what the estate has following approval of the
9 stipulation and the Trustee's sale of the estate's claims to C&S
10 is an unencumbered postpetition bargained-for contract and right
11 to payment. Both are property of the estate under § 541(a)(7) of
12 the Bankruptcy Code which includes "[a]ny interest in property
13 that the estate acquires after the commencement of the case." 11
14 U.S.C. § 541(a)(7); see also Carroll v. Tri-Growth Centre City,
15 Ltd. (In re Carroll), 903 F.2d 1266, 1270 (9th Cir. 1990)
16 (typical § 541(a)(7) property of estate is a postpetition
17 contract); In re MCEG Productions, Inc., 133 B.R. 232, 235
18 (Bankr. C.D. Cal. 1991) (postpetition compromise agreement).⁵

19 In short, C&S is obligated to pay \$429,505.00 as
20 consideration for its purchase of the estate's claims from the
21 Trustee. That payment - like the entirety of the Settlement
22 Funds - is not subject to any security interest and is property
23

24 ⁵The significance of this conclusion is discussed in Section
25 II, infra. This conclusion also raises interesting questions not
26 presently before the court, but which perhaps could be: By
27 withholding payment from the estate does the Trustee, on behalf
28 of the estate, now have a claim against C&S for violation of 11
U.S.C. § 362(a)(3) which prohibits an "act to obtain possession
of property of the estate or of property from the estate or to
exercise control over property of the estate[?]" And if C&S
violated § 362(a)(3) is it now liable to the estate for actual,
and potentially punitive, damages under 11 U.S.C. § 362(k)?

1 of the estate. Therefore, for the foregoing reasons, the court
2 will grant summary judgment for the Trustee on the First Claim
3 for Relief in the complaint and will deny summary judgment for
4 C&S on the Fourth Claim for Relief in the counterclaim.

5
6 B. The Neri Trust Account Funds are not Encumbered by
7 C&S's Security Interest.

8 This "bucket" includes the funds that were transferred from
9 DRP's bank account to Neri's client trust account in late 2010,
10 and thereafter transferred from Neri's client trust account to
11 the Trustee in 2011. DRP's bank account from which these funds
12 came is a "deposit account" within the meaning of California
13 Commercial Code § 9102(a)(29). So too is Neri's client trust
14 account. In re Allied Respiratory Care Services, Inc., 182 B.R.
15 589, 593-595 (Bankr. S.D. Fla. 1995).

16 A financing statement is not effective to perfect a security
17 interest in a deposit account. See Cal. Comm. Code § 9310(b)(8).
18 In fact, except when proceeds in a deposit account are already
19 subject to a perfected security interest under California
20 Commercial Code §§ 9315(c) and (d), a security interest in a
21 deposit account is perfected only by control. See Cal. Comm.
22 Code §§ 9312(b) & (b)(1); §§ 9314(a) & (b). A secured party has
23 control over a deposit account for purposes of perfection of a
24 security interest under any of the following conditions: (i) the
25 secured party is the bank where the funds are deposited; (ii) the
26 secured party, the debtor, and the bank enter into a deposit
27 control agreement; or (iii) the security agreement becomes the
28 bank's customer with respect to the deposit account. See Cal.

1 Comm. Code §§ 9104(a)(1)-(3).

2 C&S has produced no evidence of control over any DRP bank
3 account, much less any bank account into which inventory proceeds
4 were supposedly deposited. The same is true with regard to
5 Neri's client trust account. There is no evidence that C&S
6 exercised control over either account. For example, C&S is not
7 the bank where the funds were deposited, it produced no deposit
8 control agreement for either account, and it has not established
9 that it is a customer of the institutions where either account
10 was maintained with respect to either account. Consequently, C&S
11 has failed to establish that it has a perfected security interest
12 in DRP's bank account and in Neri's client trust account as
13 deposit accounts. But that does not end the inquiry.

14 A secured creditor can retain a perfected security interest
15 in a deposit account as proceeds to the extent funds credited to
16 the deposit account are proceeds of the secured creditor's
17 primary collateral. Stierwalt v. Associated Third Party
18 Administrators, 2016 WL 2996936, *3 (N.D. Cal. 2016). However, a
19 "transferee" of funds from a deposit account takes the funds from
20 the deposit account free of any security interest. See Cal.
21 Comm. Code § 9332. And as explained below, that includes the
22 Trustee who is, and who C&S acknowledges is, a "transferee."

23 The parties stipulated that \$560,000.00 went from DRP's bank
24 account to Neri's client trust account in late 2010. There is
25 also deposition testimony that in late 2010 inventory proceeds
26 were deposited into Neri's client trust account. Construing that
27 evidence favorably to C&S, that could mean that the funds that
28 went into Neri's client trust account in late 2010 were all

1 inventory proceeds and, as such, were subject to C&S's security
2 interest. But even if that is the case, when those funds were
3 transferred out of Neri's client trust account to the Trustee
4 they were free and clear of any security interest when received
5 by the Trustee. There are two paths to this conclusion.

6 In Orix Fin. Serv., Inc. v. Kovacs, 167 Cal. App. 4th 242
7 (Cal. App. 2008) (as modified October 16, 2008), a debtor
8 business defaulted on its financial obligation to Orix which was
9 secured by all of the business's goods, chattels, and property.
10 Id. at 246. Separately, defendant Kovacs obtained a judgment
11 against the business and executed on the business's deposit
12 account. Id. All of the funds in that deposit account were
13 proceeds from the sale of the business's inventory and collection
14 of its accounts receivables, which meant all of the deposits were
15 subject to Orix's security interest. Id. Kovacs' execution on
16 the business's deposit account prompted Orix's suit against
17 Kovacs. Id. The trial court sustained a demure by Kovacs and
18 Orix appealed. Id. at 245.

19 On appeal, Kovacs conceded that Orix's position as a secured
20 creditor was superior to its own as a judgment creditor. Id. at
21 246. However, Kovacs argued that such an analysis was irrelevant
22 to the question of the satisfaction of his judgment from the
23 funds in the business's deposit account, which it maintained was
24 wholly free of any such priority analysis because of California
25 Commercial Code § 9332(b). Id. The California appellate court
26 agreed with Kovacs and held that, as a judgment creditor, Kovacs
27 was a transferee under California Commercial Code § 9332(b) who
28 took funds from the business's deposit account free and clear of

1 any security interest. Id. at 245, 251. Notably, the court
2 supported its holding by reference to Harley-Davidson Motor Co.
3 v. Bank of New England-Old Colony N.A., 897 F.2d 611, 622 (1st
4 Cir. 1990), in which U.S. Supreme Court Justice Breyer referred
5 to comment 2(c) of U.C.C. § 9-306 from which California
6 Commercial Code § 9332(b) is derived to note that the purpose
7 behind § 9-306 was (and thence § 9332(b) is) to explicitly
8 exclude any judicial efforts to trace identifiable secured
9 proceeds paid out of a commingled deposit account. Orix
10 Financial, 167 Cal. App. 4th at 248.

11 More recently, Stierwalt, supra, involved a similar dispute
12 between a judgment creditor who levied on funds in the judgment
13 debtor's bank account and a secured creditor who claimed a
14 security interest in the judgment debtor's bank account as a
15 deposit account and as proceeds of its collateral. Stierwalt,
16 2016 WL 2996936 at *1, *2. In the absence of the requisite
17 control, the court concluded that the secured creditor lacked a
18 perfected interest in the bank account as a deposit account. Id.
19 at *3. More importantly, the court recognized that the proceeds
20 in the bank account were identifiable proceeds and, as such,
21 subject to the secured creditor's security interest as proceeds
22 of its contract rights collateral. Id. at *4-*5. Nevertheless,
23 relying on Orix Financial, the court concluded that the secured
24 creditor's security interest in the funds as proceeds of its
25 contract rights collateral did not survive the transfer of those
26 funds out of the deposit account to the judgment creditor who, as
27 in Orix Financial, was a transferee under California Commercial
28 Code § 9332(b). Id. at *6-*8.

1 The Trustee cites Orix Financial to support her position
2 that the \$384,000.00 transferred to her from Neri's client trust
3 account is not encumbered by C&S's security interest. In
4 response to that argument, C&S acknowledges that Orix Financial
5 holds that a judgment creditor is a transferee under § 9332(b) of
6 the California Commercial Code who takes funds from a deposit
7 account free and clear. However, C&S maintains that Orix
8 Financial and § 9332(b) are inapplicable because the Trustee is
9 not, and when she received the \$384,000.00 from Neri's client
10 trust account was not, a judgment creditor. More precisely, C&S
11 states as follows:

12 [T]he Trustee cites [Orix], but as the Orix court
13 explained, 'This case presents a very narrow
14 question-one of first impression in California: Is an
15 unsecured judgment creditor, who satisfied its judgment
16 from deposit account funds, included in the definition
17 of a 'transferee' as contemplated by section 9332(b),
18 such that it may take those funds free of any security
19 interest?' Id. at 245. The court held that the answer
to that question was 'yes.' In other words, an
unsecured judgment creditor may satisfy its judgment
from deposit accounts [sic] funds and take such funds
'free and clear.' But it is undisputed that the
Trustee was not a judgment creditor and did not obtain
what remained of the \$560,000 by way of a lawsuit and
subsequent satisfaction of judgment.

20 Dkt. 71 at 15:14-16. And that is where C&S's argument collapses.

21 C&S fails to recognize that § 544(a) of the Bankruptcy Code
22 confers upon the Trustee the status of a hypothetical judgment
23 creditor and lienholder as of the date a bankruptcy petition is
24 filed. See 11 U.S.C. § 544(a); Neuton v. Danning (In re Neuton),
25 922 F.2d 1379, 1383 (9th Cir. 1990); In re Lloyd, 511 B.R. 657,
26 659 (Bankr. D. Ariz. 2014). Thus, as C&S acknowledges and Orix
27 Financial and Stierwalt hold, that makes the Trustee a transferee
28 under § 9322. And that means the Trustee took the Neri Trust

1 Account Funds from Neri's client trust account free and clear of
2 any existing security interest. Therefore, for the foregoing
3 reasons, the court will grant summary judgment for the Trustee on
4 the Fourth Claim for Relief in the complaint and will deny
5 summary judgment for C&S on the First Claim for Relief in the
6 counterclaim.

7 Alternatively, it is true as C&S points out, a security
8 interest attaches to identifiable proceeds of collateral. See
9 Cal. Comm. Code § 9315(a)(2). It also is true that a security
10 interest in proceeds is perfected if the security interest in the
11 original collateral was perfected. See Cal. Comm. Code §
12 9315(c). However, a security interest in proceeds only remains
13 perfected for twenty days and becomes unperfected on the twenty-
14 first day unless one of three conditions is satisfied. See Cal.
15 Comm. Code § 9315(d).

16 The first condition applies to maintain perfection if (i) a
17 filed financing statement covers the original collateral, (ii)
18 the proceeds are collateral that could be perfected by filing a
19 financing statement, and (iii) the proceeds are not acquired with
20 cash proceeds. See Cal. Comm. Code § 9315(d)(1)(A)-(C). Here,
21 the proceeds are either cash or a deposit account. A security
22 interest in either is not perfected by a financing statement.
23 The former requires possession for perfection, see Cal. Comm.
24 Code §§ 9312(b)(3) & 9313(a), and, as explained above, the latter
25 requires control for perfection. There is no evidence that C&S
26 took possession of any inventory cash proceeds (the testimony is
27 that they were deposited into bank accounts) and, as noted above,
28 there is no evidence that C&S had control over any deposit

1 account. Thus, while a security interest in the original
2 collateral, i.e., inventory, could be perfected by a financing
3 statement, a security interest in proceeds of that collateral,
4 i.e., cash or a deposit account, could not. Consequently, the
5 first condition is not satisfied.

6 The second condition is also not satisfied. The second
7 condition allows perfection to be maintained in "identifiable
8 proceeds." See Cal. Comm. Code § 9315(a)(2). However, once cash
9 proceeds are deposited into an account and commingled with other
10 money the identifiability of a secured creditor's proceeds is
11 destroyed unless the secured creditor can prove that the money in
12 the account corresponds to its collateral. Arkison v. Frontier
13 Asset Mgmt., LLC (In re Skagit Pacific Corp.), 316 B.R. 330, 338
14 (9th Cir. BAP 2004). That is done by tracing proceeds in the
15 commingled account to the collateral. See Cal. Comm. Code §
16 9315(b)(2). The burden of tracing rests with the secured
17 creditor claiming a security interest in the proceeds. Id.
18 (citing Stoumbos v. Kilimnik, 988 F.2d 949, 957 (9th Cir. 1993));
19 Chrysler Credit Corp. v. Superior Court, 17 Cal. App. 4th 1303,
20 1311 (Cal. App. 1993). The secured creditor meets that burden by
21 submitting detailed testimony or documentary evidence that
22 establishes a transactional link between the proceeds and the
23 collateral. Arkinson, 316 B.R. at 338 (citing Stoumbos, 988 F.2d
24 at 958); see also In re Sunrise R.V., Inc., 107 B.R. 277, 282
25 (Bankr. E.D. Cal. 1989).

26 The burden here is on C&S, as the secured creditor claiming
27 a security interest in the funds transferred from Neri's client
28 to the Trustee, to establish those funds are proceeds of its

1 inventory collateral. Evidence of tracing, if it can be
2 considered that, is limited to conclusory and speculative
3 deposition testimony that inventory proceeds went into Neri's
4 client trust account in late 2010 and a spreadsheet that reflects
5 "approximately five deposits" over a three-month period between
6 October and December 2010. Even if that sufficed to establish
7 what went into Neri's client trust account, it does not establish
8 a link between the funds that Neri transferred from his client
9 trust account to the Trustee back to C&S's original inventory
10 collateral. In other words, it is not *detailed* evidence of
11 tracing.

12 For example, there is no evidence that once in Neri's client
13 trust account inventory proceeds were and remained segregated.
14 In fact, the same deposition testimony on which C&S relies to
15 establish that inventory proceeds went into Neri's client trust
16 account also reflects that once in that account the inventory
17 proceeds were commingled with at least \$100,000.00 in other funds
18 that did not belong to DRP and some other unidentified
19 operational funds. Moreover, because \$100,000.00 in the account
20 did not belong to DRP and belonged to someone named "Peterson,"
21 sometime after inventory proceeds were deposited in Neri's client
22 trust account and thereafter commingled with other funds in that
23 account Neri transferred \$100,000.00 to a separate "Peterson"
24 account. But what \$100,000.00 did Neri transfer? C&S does not
25 answer that question with any admissible evidence. And what of
26 the other operational funds in the account - what where they and
27 where did they come from? Again, C&S does not answer those
28 questions with admissible evidence.

1 The problem for C&S is that there is no detailed evidence in
2 the form of deposition testimony or documentation that traces the
3 \$384,000.00 that was transferred to the Trustee in 2011 back
4 through Neri's client trust account to funds apparently
5 transferred from DRP's bank account and finally back to proceeds
6 of original inventory collateral. Thus, even if all the deposits
7 that went into Neri's client trust account in late 2010 were
8 inventory proceeds going in, C&S has failed to establish they
9 remained identifiable in the account and when thereafter
10 transferred out of the account. Consequently, the second
11 condition is also inapplicable.

12 The third condition is the simplest. If the proper steps
13 for perfecting a security interest in the type of collateral that
14 constitutes proceeds are taken before the twenty-first day after
15 the security interest attaches to the proceeds, perfection is
16 maintained. See Cal. Comm. Code. § 9315(d)(3). Again, there is
17 no evidence that C&S ever took possession of any inventory
18 proceeds within twenty days of any inventory sales and, as
19 explained above, there is no evidence it had control over any
20 deposit account. Accordingly, this third condition is likewise
21 inapplicable.

22 In sum, and alternatively, even if the Neri Trust Account
23 Funds were proceeds of DRP's inventory collateral when they went
24 into Neri's client trust account in late 2010, there is no
25 evidence that C&S retained a perfected security interest in those
26 proceeds in 2011 when they were transferred out of the trust
27 account to the Trustee. That would mean when the funds were
28 transferred from Neri's client trust account to the Trustee in

1 2011, at best, C&S would have had an unperfected security
2 interest in the inventory proceeds. That would also mean that,
3 as a hypothetical judgment creditor and lienholder under §
4 544(a), the Trustee's interest in the Neri Trust Account Funds
5 would be superior to C&S's unperfected security interest in the
6 same funds. Therefore, on this alternative basis, the court
7 would grant summary judgment for the Trustee on the Fourth Claim
8 for Relief in the complaint and deny summary judgment for C&S on
9 the First Claim for Relief in the counterclaim.

10
11 C. The Asset Lease Funds are not Encumbered by C&S's
12 Security Interest.

13 The Asset Lease is chattel paper. NetBank, FSB v. Kipperman
14 (In re Commercial Money Center, Inc.), 350 B.R. 465, 469 (9th
15 Cir. BAP 2006) ("Commercial Money I"). The security agreement
16 between C&S and DRP grants C&S a security interest in chattel
17 paper. C&S perfected its interest in chattel paper with a
18 properly filed financing statement. See Cal. Comm. Code §
19 9312(a). But here, at least with respect to payments under the
20 Asset Lease collected directly by the Trustee, we're not dealing
21 with chattel paper.

22 In Commercial Money I, the bankruptcy appellate panel held
23 that there is a critical distinction between a lease and a
24 payment stream under a lease when the payment stream is stripped
25 from the lease and paid to a third-party. When the payment
26 stream is stripped from the lease and paid to a third party, the
27 bankruptcy appellate panel held that the payment stream is no
28 longer chattel paper but, instead, becomes a newly-created, and a

1 wholly separate and distinct, payment intangible which is a
2 subset of general intangibles. Id. at 469, 476, 478; Federal
3 Deposit Ins. Corp. v. Kipperman (In re Commercial Money Center,
4 Inc.), 392 B.R. 814, 824 (9th Cir. BAP 2008) ("Commercial Money
5 II"). This critical distinction is explained in context below.

6 "Th[e] estate and the Chapter 7 trustee appointed to
7 administer the estate are separate and distinct entities from the
8 pre-petition debtor." In re Central Louisiana Grain Co-Op, Inc.,
9 467 B.R. 390, 396 (Bankr. W.D. La. 2012). That legal distinction
10 is crucial because it means that when DRP filed its bankruptcy
11 petition a new legal entity in the form of the estate was created
12 by operation of federal law. That also means when the Trustee
13 thereafter collected the lease payments under the Asset Lease
14 directly from 2040 FF and on behalf of the estate the payment
15 stream under the Asset Lease was paid to a separate legal entity
16 and thereby stripped from the original payee under the lease
17 agreement. That did two things.

18 First, stripping the lease payments from the Asset Lease and
19 paying them directly to the estate as a third party made the
20 payment stream a new and distinct postpetition intangible that
21 did not exist prepetition when the payment stream remained with
22 the Asset Lease, i.e., was paid to DRP. Second, as a newly-
23 created postpetition payment intangible that did not exist
24 prepetition, the Asset Lease payment stream was not (and could
25 not have been) encumbered by C&S's prepetition security interest.
26 See 11 U.S.C. § 552(a). Nor could it have been proceeds,
27 products, offspring or profits of prepetition collateral. See 11
28 U.S.C. § 552(b)(1). In fact, perfecting an interest in the

1 postpetition payment stream as a payment intangible would have
2 required C&S to file a financing statement that covered it, see
3 In re Commercial Money Center, Inc., 2007 WL 7144803, *3-4
4 (Bankr. S.D. Cal. 2007) (on remand from Commercial Money I, 350
5 B.R. 465), aff'd, Commercial Money II, 392 B.R. 814, which C&S
6 did not do.

7 In sum, the \$153,410.08 in postpetition Asset Lease payments
8 collected directly by the Trustee are not C&S's collateral or
9 proceeds of its collateral, which means those payments are not
10 subject to C&S's security interest. Therefore, the court will
11 grant summary judgment for the Trustee on the Third Claim for
12 Relief in the complaint and will deny summary judgment for C&S on
13 the Second Claim for Relief in the counterclaim.

14
15 D. The Liquor License Funds are not Encumbered by C&S's
16 Security Interest.

17 California law prohibits the use of a liquor license as
18 collateral for a loan. California Business & Professions Code §
19 24076 states that "[n]o licensee shall enter into any agreement
20 wherein he pledges the transfer of his license as security for a
21 loan or as security for the fulfillment of any agreement[.]" See
22 also In re Morev, 2015 WL 9264937, *4 (Bankr. S.D. Cal. 2015).
23 And perhaps that is why C&S does not assert a security interest
24 *directly* in the liquor licenses sold by the Trustee. Instead,
25 C&S maintains that DRP's liquor licenses are general intangibles
26 which makes the funds that the Trustee received from the sale of
27 those liquor licenses proceeds of its collateral and thereby
28 subject to its security interest. C&S relies primarily on two

1 cases: Concorde Equity II, LLC v. Bretz, 2011 WL 5056295 (Cal.
2 App. 2011), and Mola Dev. Corp. v. Orange County Assessment
3 Appeals Bd., 80 Cal. App. 4th 309 (Cal. App. 2000). Neither are
4 persuasive.

5 An analysis of this issue must begin with Sulmeyer v.
6 California Dept. of Employment Dev. (In re Professional Bar Co.),
7 537 F.2d 339 (9th Cir. 1976) (per curium), in which the Ninth
8 Circuit stated as follows: "The bankrupt estate, insofar as it
9 includes liquor licenses, has only the limited value of the
10 licenses encumbered as they may be by the terms of the statutes
11 which create the licenses and provide the conditions of their
12 transfer." Id. at 340. And on that basis, Concorde Equity is
13 not helpful or persuasive. More important, it is not applicable.

14 Concorde Equity involved a priority dispute under California
15 Business & Professions Code § 24074 over proceeds from the sale
16 of a liquor license claimed by two judgment creditors. Concorde
17 Equity, 2011 WL at *1. The sale proceeds were insufficient to
18 satisfy both creditors' claims against the judgment debtor/liquor
19 license owner. Id. Therefore, in order to determine which
20 creditor had priority to the proceeds from a receiver's sale of
21 the liquor license *for purposes of distribution under California*
22 *Business & Professions Code § 24074*, the court characterized the
23 proceeds as a business asset of the judgment debtor, which made
24 the judgment creditor with a pre-existing security interest in
25 the judgment debtor's business assets a "secured creditor" for
26 purposes of third priority distribution under § 24074. Id. at
27 *3.

28 The problem with Concorde Equity is that both federal and

1 California courts recognize that its analysis does not apply
2 inside a bankruptcy case. Citing Gough v. Finale, 39 Cal. App.
3 3d 777, 783-84 (Cal. App. 1974), the Ninth Circuit in
4 Professional Bar also stated as follows: "Although Cal. Bus. and
5 Prof. Code § 24074 (West Supp. 1975) establishes a system of
6 priorities among creditors in the transfer of a state liquor
7 license, federal rather than California law must be applied in
8 deciding priority when the net proceeds in issue have become
9 available to the [bankruptcy] trustee." Id. at 340. In other
10 words, Professional Bar's reliance on Gough is convincing
11 evidence that Concorde Equity is a state law priority
12 distribution case and, as such, its analysis is inapplicable in
13 this federal bankruptcy case.

14 As to Mola, it is true that the court in that case made a
15 passing reference to a liquor license as an intangible. Mola,
16 however, is a taxation case. And just because a liquor license
17 may be characterized as an intangible under state tax law, that
18 does not necessarily mean it is an intangible under the Uniform
19 Commercial Code for bankruptcy purposes.

20 In order for a liquor license or its proceeds to qualify as
21 general intangible under Article 9 in the context of a bankruptcy
22 case, and thereby subject to a security interest as such, the
23 liquor license must first qualify as personal property under
24 state law. See In re Circle 10 Restaurant, LLC, 519 B.R. 95, 128
25 (Bankr. D.N.J. 2014). This is because Article 9 defines a
26 "general intangible" as "any personal property." Cal. Comm. Code
27 § 9102(a)(42). Thus, in states where a liquor license is not
28 property under state law, it also is not (and cannot be) a

1 general intangible under the state's version of Article 9. See,
2 e.g., Circle 10, 519 B.R. at 135-37; In re Chris-Don, Inc., 367
3 F. Supp. 696, 699 (D.N.J. 2005). On the other hand, in states
4 where a liquor license is personal property under state law, a
5 liquor license can be a general intangible subject to an Article
6 9 security interest. See, e.g., In re Ciprian Ltd., 473 B.R 669,
7 672 (Bankr. W.D. Pa. 2012). Therefore, the threshold question is
8 whether DRP's liquor licenses are personal property under
9 California law for purposes of applying the California Commercial
10 Code in this bankruptcy case. This court is not persuaded that
11 they are.

12 The court is aware that there are some federal and state
13 cases that characterize a California liquor license as
14 "property." However, they do so in the context of a *federal*
15 statute and for *federal* law purposes. See e.g., Golden v. State,
16 133 Cal. App. 2d 640, 643-45 (1955) (for purposes of federal tax
17 lien under federal tax law); Dash, Inc. v. Alcoholic Beverage
18 Control Appeals Bd., 683 F.2d 1229, 1233 (9th Cir. 1982) (for
19 purposes of federal due process analysis). Characterization of a
20 liquor license as property for *federal* law purposes in general,
21 and particularly for federal tax and due process purposes, does
22 not mean that a liquor license is property under *state* law in
23 general and for purposes of defining the scope of intangibles
24 under a state's commercial code in particular, at least in the
25 context of a bankruptcy case. Circle 10, 519 B.R. at 133. That
26 is because the bankruptcy code is unlike the tax code or federal
27 due process analysis because under Butner v. United States, 440
28 U.S. 48 (1979), what is "property" for the "federal purpose" of

1 the bankruptcy code is defined by state law.⁶ See Circle 10, 519
2 B.R. at 133.

3 In determining whether a California liquor license is
4 personal property under California state law for purposes of the
5 commercial code, one could argue that California law draws a
6 distinction between rights as between the licensee and the state
7 and rights as between the licensee and a third party. That
8 distinction seems to find some support in Roehm v. County of
9 Orange, 32 Cal. 2d 280 (1948), in which the California Supreme
10 Court stated: "Although a liquor license is merely a privilege
11 so far as the relations between the licensee and the state are
12 concerned, it is property in any relationship between the
13 licensee and third persons, because the license has value and may
14 be sold." Id. at 283. But after noting that distinction, which
15 actually appears to be the court's recitation of a party's
16 argument, the California Supreme Court ultimately rejected it.
17 Instead, the supreme court framed the question before it as
18 follows: "The controlling question is whether under present
19 constitutional and statutory provisions such [liquor] licenses
20 can now be regarded as personal property for the purposes of
21 taxation." Roehm, 32 Cal. 2d at 284. It answered that question
22 in the negative concluding that a liquor license is not taxable
23 personal property under state law. Id. at 290 ("Although liquor
24 licenses are not taxable as property...."). Thus, Roehm holds
25

26 ⁶This should not be confused as to what is "property of the
27 estate" for the federal bankruptcy purpose. A California liquor
28 license is property of the estate under 11 U.S.C. § 541(a) for
the federal purpose of bankruptcy. In re Quaker Room, 90 F.
Supp. 758, 760-61 (S.D. Cal. 1950).

1 that a liquor license, albeit an intangible for state taxation
2 purposes, is not taxable (or taxed as) personal property under
3 state constitutional and statutory provisions. See American
4 Sheds, Inc. v. County of Los Angeles, 66 Cal. App. 4th 384, 392
5 (Cal. App. 1988).

6 The California legislature and numerous California cases
7 also describe a liquor license not as a "right" but as a
8 "privilege" conferred by state law. See California Business &
9 Professions Code § 24079 (describing alcoholic beverage license
10 as a "privilege"); Hevren v. Reed, 126 Cal. 219, 222 (Cal. 1899)
11 (liquor license is neither property nor a contract, in any
12 constitutional sense); Yu v. Alcoholic Bev. Etc. Appeals Bd., 3
13 Cal. App. 4th 286, 297 (Cal. App. 1992) ("While a license to
14 practice a trade is generally considered a vested property right,
15 a license to sell liquor is a *privilege* that can be granted or
16 withheld by the state."); Cornell v. Reilly, 127 Cal. App. 2d
17 178, 184 (Cal. App. 1954) (proceeding to revoke liquor license is
18 not for the primary purpose of punishment but "to protect the
19 public, that is, to determine whether a licensee has exercised
20 his *privilege* in derogation of the public interest, and to keep
21 the regulated business clean and wholesome"); Saso v. Furtado,
22 104 Cal. App. 2d 759, 763-64 (Cal. App. 1951) (explaining that a
23 liquor license is a privilege rather than a state law, contract,
24 or constitutional right).

25 The court also finds unpersuasive the argument that a liquor
26 license has value apart from the license which transforms the
27 license into personal property and thence into a general
28 intangible under the California Commercial Code. The court in

1 Circle 10 addressed that issue under New Jersey law, which
2 characterizes a liquor license as a privilege and not personal
3 property under state law but also recognizes that a liquor
4 license and its transferability have value to the licensee. The
5 Circle 10 court resolved that conflict by reasoning that any
6 value to the licensee is created and exists solely as a result of
7 the issuance of the license by the state and therefore cannot be
8 bifurcated from the license itself. Circle 10, 519 B.R. at 131-
9 32. Thus, the Circle 10 court ultimately concluded that any
10 value to the licensee did not make the liquor license personal
11 property and that, in turn, meant that proceeds from the sale of
12 the license could not be subject to a security interest as a
13 general intangible. Id. at 132. That analysis is persuasive.
14 Like New Jersey, the value that a California liquor license has
15 to a licensee is created by and exists only as a result of the
16 issuance of the license by the state. That makes the value
17 inseparable from the license.

18 In sum, a California liquor license is not personal property
19 under state law for purposes of defining it as a general
20 intangible under the California Commercial Code in a bankruptcy
21 case. That means the Liquor License Funds in the approximate
22 amount of \$37,661.60 are not (and cannot be) collateral subject
23 to C&S's security interest. Put another way, DRP's liquor
24 licenses are not general intangibles under the California
25 Commercial Code because in the context of this bankruptcy case
26 they are not personal property under state law. Therefore, the
27 court will grant summary judgment for the Trustee on the Second
28 Claim for Relief in the complaint and will deny summary judgment

1 for C&S on the Third Claim for Relief in the counterclaim.

2
3 II. The Trustee's § 542(a) Turnover Claim

4 C&S maintains the stipulation does not state when it has to
5 pay the Trustee. That may be the case. But the Bankruptcy Code
6 does insofar as property of the estate is concerned.

7 An entity, other than a custodian, in possession, custody,
8 or control, during the case, of property of the estate *shall*
9 deliver to the trustee, and account for, the property or the
10 value of the property unless the property is of inconsequential
11 value. 11 U.S.C. § 542(a). Section 542(a) "creates an
12 affirmative obligation on the part of the party holding estate
13 property to turn the property over[.]" In re Rutheford, 329 B.R.
14 886, 892 (Bankr. N.D. Ga. 2005). Moreover, "[t]his affirmative
15 obligation is self-executing and does not require the holding of
16 a hearing or the entry of an order by the bankruptcy court." In
17 re Prince, 2012 WL 1095506, *9 (Bankr. E.D. Tex. 2012) (citing
18 Knaus v. Concordia Lumber Co. (In re Knaus), 889 F.2d 773, 775
19 (8th Cir. 1989); Boyer v. Carlton, Fields, Ward, Emmanuel, Smith
20 & Cutler, P.A. (Matter of USA Diversified Products, Inc.), 100
21 F.3d 53, 56 (7th Cir. 1996)).

22 The court concludes that \$429,505.00 is not of
23 inconsequential value. And inasmuch as the court has determined
24 that the May 2013 stipulation and the payment that the Trustee is
25 entitled to receive under that agreement are property of the
26 estate, as a matter of law C&S now has an affirmative obligation
27 to turn over \$429,505.00 to the Trustee. And while C&S may think
28 the timing of that turnover obligation is in dispute because the

1 stipulation is silent on that point, that is a non-issue. The
2 Ninth Circuit has long-recognized that "[i]t is well settled that
3 existing laws are read into contracts in order to fix the rights
4 and obligations of the parties." Rehart v. Clark, 448 F.2d 170,
5 173 (9th Cir. 1971). In other words, the Bankruptcy Code fills
6 in any gap or any silence in the stipulation with regard to the
7 timing of C&S's payment obligation which, as noted, is an
8 affirmative obligation on the part of C&S to turn over to the
9 Trustee the Settlement Funds as property of the estate.
10 Therefore, for the foregoing reasons, the court will grant
11 summary judgment for the Trustee on the § 542(a) turnover claim
12 in the Fifth Claim for Relief of the complaint. C&S is ORDERED
13 to turn over \$429,505.00, or such portion of the Settlement Funds
14 currently in its possession, to the Trustee within ten days of
15 the entry of judgment.

16
17 **CONCLUSION**

18 For all the foregoing reasons, the Trustee's motion for
19 summary judgment will be granted and judgment will be entered for
20 the Trustee and against C&S on the First, Second, Third, Fourth,
21 and Fifth Claims for Relief in the complaint. C&S's motion for
22 summary judgment will be denied and C&S will take nothing on the
23 First, Second, Third, and Fourth Claims for Relief in the
24 counterclaim.

25 Dated: August 14, 2017.

26
27 
28 UNITED STATES BANKRUPTCY JUDGE

1
2 INSTRUCTIONS TO CLERK OF COURT
3 SERVICE LIST

4 The Clerk of Court is instructed to send the attached
5 document, via the BNC, to the following parties:

6 Howard S. Nevins
7 2150 River Plaza Dr #450
8 Sacramento CA 95833-3883

9 Michael J. Stortz
10 50 Fremont St 20th Fl
11 San Francisco CA 94105

12 Paul J. Pascuzzi
13 400 Capitol Mall #1750
14 Sacramento CA 95814
15
16
17
18
19
20
21
22
23
24
25
26
27
28